Supreme Court, U.S.
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No. 85-1558

In The
Supreme Court of the United States
October Term, 1985

EMPIREGAS, INC. OF ARDMORE,
Petitioner,

vs.

VERNON HARDY AND LINDA GAIL COFFMAN,
Respondents.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF ALABAMA

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QUESTIONS PRESENTED

I. Whether this Court is without jurisdiction to review a state court judgment when the question which the Petitioner seeks to have reviewed was not properly raised or passed upon in the state court below?

II. Whether this Court is without jurisdiction to review a state court judgment because no substantial federal question is presented, when the state court judgment was decided wholly on the basis of state law and no federal question was raised or passed upon below?

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STATEMENT OF THE CASE

The Respondents brought suit against their employer, the Petitioner, in the Circuit Court for Limestone County, Alabama, alleging that the Petitioner wrongfully interfered with the Respondents' employment opportunities, fraudulently induced the Respondents to sign employment contracts containing noncompetition provisions, and fraudulently concealed material information concerning the proposed merger of Empire, Inc. and Exco Acquisition Corp. The jury found in the favor of the Respondents on their claim for fraud and wrongful interference with employment opportunities. As to the Respondent, Coffman, the jury assessed damages of $3670 for wrongfully preventing her from securing employment and $29,670 for fraud (Pet. Appendix A, p. 3a). As to Respondent, Hardy, the jury assessed damages of $16,-200 for wrongfully preventing him from securing employment and $70,822.15 for fraud (Pet. Appendix A, p. 3a). The Petitioner never raised any question concerning alleged preemption of the Respondents' state law fraud claims under Section 514(a) of the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C.S. § 1144 (a) (1982) during the trial court proceedings (Pet. 2).

On appeal to the Alabama Supreme Court, the Petitioner again failed to raise the claimed question of preemption of the Respondents' fraud claims under ERISA (Pet. 2); consequently, the Alabama Supreme Court's opinion does not mention, discuss, or decide the question of preemption under ERISA (Pet. Appendix A). The Alabama Supreme Court affirmed the trial court's judgment in favor of the Respondents. The Alabama Supreme Court simply decided this case solely on the basis of Ala-

bama law and found that the Respondents presented sufficient evidence under Alabama law to support instructing the jury as to fraud and wrongful interference with employment opportunities.

The Petitioner filed an Application for Rehearing with the Alabama Supreme Court, but still did not raise any question of preemption under ERISA. The Petitioner's Application for Rehearing was subsequently summarily denied by the Alabama Supreme Court (Pet. Appendix C). In its Petition for Writ of Certiorari to this Court, the Petitioner raised, *for the very first time,* the claimed question of preemption under ERISA.

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REASONS FOR DENYING THE WRIT

I. The Question Which The Petitioner Seeks To Have Reviewed Was Not Propertly Raised Or Passed Upon By The State Courts Below.

The Petitioner in this case contends that the Respondents' state law fraud claims were preempted by Section 514(a) of the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C.S. § 1144(a) (1982). The Petitioner, however, did not raise this question either in the trial court or in the Alabama Supreme Court (Pet. 2). This Court has consistently ruled that it is without jurisdiction to consider federal questions which were not raised or passed upon in the state courts. *Heath v. Alabama,* 106 S. Ct. 433, 436-437 (1985); *Webb v. Webb,* 451 U.S. 493, 495 (1981); *Cardinale v. Louisiana,* 394 U.S. 437, 439 (1969).

The opinion of the Alabama Supreme Court (Pet. Appendix A), which was decided solely on the basis of

state law, does not mention, discuss, or decide any federal questions. This Court has frequently held "that when 'the highest state court has failed to pass upon a federal question, it will be assumed that the omission was due to want of proper presentation in the state courts, unless the aggrieved party in this Court can affirmatively show to the contrary.'" *Webb*, 451 U.S. at 495; *Street v. New York*, 394 U.S. 576, 582 (1969). The Petitioner has made no such showing in the present case; in fact, the Petitioner even expressly admits that the preemption question was never raised at any point in the state court proceedings (Pet. 2).

The Petitioner contends that it preserved the preemption issue for review by objecting to the submission of punitive damages to the jury (Pet. 2). The Petitioner, however, only objected to the submission of punitive damages to the jury on the grounds that *under Alabama law* the Petitioner's actions could not be characterized as malicious, willful or wanton. The Alabama Supreme Court, also, requires that issues be raised in the trial court and will not consider issues raised for the first time on appeal. *Green v. Taylor*, 437 So.2d 1259, 1260 (Ala. 1983); *Smiths Water Auth. v. City of Phenix City*, 436 So.2d 827, 830 (Ala. 1983).

This Court has identified "powerful policy considerations" underlying the "properly-raised-federal-question" doctrine. *Webb*, 451 U.S. at 499 and 500. First, principles of comity in our federal system "require that the state courts be afforded the opportunity to perform their duty, which includes responding to attacks on state authority based on the federal law, or, if the litigation is wholly private, construing and applying the applicable

federal requirements." 451 U.S. at 499. "[D]ue regard for the appropriate relationship of this Court to state courts" requires that this Court review state court decisions only where the federal question has been properly raised below. *McGoldrick v. Compagnie Generale,* 309 U.S. 430, 435-436 (1940).

Secondly, the requirement that federal questions be presented first in the state court system "affords the parties the opportunity to develop the record necessary for adjudicating the issue." *Webb,* 451 U.S. at 500. This Court has recognized that "questions not raised below are those on which the record is very likely to be inadequate since it certainly was not compiled with those questions in mind." *Illinois v. Gates,* 103 S.Ct. 2317, 2323 (1983) (quoting from *Cardinale,* 394 U.S. at 439).

The rule also insures "that if there are independent and adequate state grounds that would pretermit the federal issue, they will be identified and acted upon in an authoritative manner." *Webb,* 451 U.S. at 500. Although state courts are not free to avoid federal questions on inadequate state grounds, "they should be given the first opportunity to consider them." *Cardinale,* 394 U.S. at 439. Finally, compliance with the rule results in a lessened workload for this Court because the state court judgment normally will be supported by an opinion "that may well obviate any reason for our giving plenary consideration to the case." *Webb,* 451 U.S. at 501.

The Petitioner's failure to raise the preemption question below in the Alabama Courts denied those courts any opportunity to consider or act on the preemption question. As a consequence, the record is devoid of any evi-

dence on the point, and there was no active search for an adequate state ground which avoids the federal question. For example, in the present case, the record contains no finding by the Alabama Courts that the employee stock ownership plan in the present case was an "employee benefit plan" within 29 U.S.C.S. § 1002 (1982) and subject to the provisions of ERISA. In fact, Petitioner never even made any such contention throughout the litigation in the trial court and the Alabama Supreme Court (Pet. 2). Respondents' compensation for their employment by Petitioner was based, in fact, on the profits of Petitioner, their employer. Such profits would naturally be adversely affected by a merger perpetrated by fraud. Respondent Hardy personally owned some Empire, Inc. stock outside the employee stock ownership plan. Thus, the merger was of interest to the Respondents for reasons completely unrelated to the employee stock ownership plan.

The Petitioner also fails to show whether the Respondents' fraud recovery was solely for the fraud perpetrated on the Respondents in connection with the merger. That is, the recovery for fraud may just as well have been for the fraud in connection with the employment contracts (See Pet. Appendix A, Page 3a). Additionally, there was never any contention in the Alabama Courts that the plan, the plan's administrator, or any of the plan's agents had any connection with the fraud.

The Petitioner contends that this Court should make an exception to the rule that federal questions be presented first in the state court system because the question involved here is the preemption of state law (Pet. 3). This Court, however, has held that it has no jurisdiction to consider whether a federal statute preempted state law

where the preemption question was not raised in the trial court or decided in the state appellate court. *Exxon Corp. v. Eagerton*, 103 S.Ct. 2296, 2300-2301 n.3 (1983). Accordingly, in the present case, this Court is without jurisdiction to consider whether the Respondents' state law fraud claims were preempted under ERISA, due to the Petitioner's complete failure to raise the preemption question in the state courts. The practical policy reasons underlying this rule, such as an inadequate record, further justify denial of the petition for writ of certiorari.

II. The Decision Of The Alabama Supreme Court Is Clearly Correct, And This Case Presents No Substantial Federal Question.

At all stages in the state court proceedings, this case has involved only the Respondents' state law claims against the Petitioner and was decided solely on the basis of state law. It it well established that this Court's jurisdiction to review a state court decision is dependent upon the presence of a federal question, and this Court has no power to review a state court decision on questions of state law. *Webb*, 451 U.S. at 494 n.1; *Henry v. State of Mississippi*, 379 U.S. 443, 447 (1965); 28 U.S.C.S. § 1257 (1977). Since the Alabama Supreme Court's decision in this case was decided wholly on the basis of state law, and the Petitioner raised no federal questions in the Alabama Courts, no federal question is present in the Alabama Supreme Court's decision, thereby precluding review by this Court.

However, even if Petitioner had properly presented the preemption question to the state courts, the Respondents' state law claims against their employer, the Peti-

tioner, were not preempted under ERISA. The trial court and the Alabama Supreme Court found that the Petitioner wrongfully interfered with the Respondents' employment opportunities, fraudulently induced the Respondents to sign employment contracts containing noncompetition provisions, and fraudulently concealed material information concerning the merger of Empire, Inc. and Exco Acquisition Corp. (Pet., Appendix A, B).

As to Respondents' claims for fraudulent concealment, the Alabama Courts found that the Petitioner fraudulently concealed the effect of the merger on the Respondents' shares of stock in Empire, Inc. to induce its employees to vote yes on their proxy cards, enabling the holder of the proxies to vote all shares in favor of the merger. Thus, the Petitioner fraudulently concealed from its employees material information concerning the merger in order to effectuate or accomplish the merger.

The Petitioner contends that the Respondents' state law claims for fraudulent concealment were preempted by Section 514(a) of ERISA, 29 U.S.C.S. § 1144(a) (1982) as relating to an "employee benefit plan" (Pet. 3-9). The record, however, contains no finding by the Alabama Supreme Court that this particular employee stock ownership plan was an "employee benefit plan" subject to the provisions of ERISA, due to the Petitioner's failure to raise the preemption issue in the state courts.

Moreover, the preemptive scope of ERISA is "neither all-encompassing [citation omitted], nor unlimited." *Rebaldo v. Cuomo*, 749 F.2d 133, 138 (2d Cir. 1984), *cert. denied*, 105 S. Ct. 2702 (1985); *Lane v. Goren*, 743 F.2d 1337, 1339 (9th Cir. 1984). This Court has recognized that "[s]ome state actions may affect employee benefit

plans in too tenuous, remote, or peripheral a manner to warrant a finding that the law 'relates to' the plan." *Shaw v. Delta Air Lines, Inc.*, 103 S.Ct. 2890, 2901 n.21 (1983). Additionally, this Court "must also presume that [in enacting ERISA] Congress did not intend to pre-empt areas of traditional state regulation." *Metropolitan Life Insurance Co. v. Massachusetts*, 105 S.Ct. 2380, 2389 (1985).

The Respondents' state law fraudulent concealment claims fall into the category of state actions which impact upon ERISA employee benefit plans in too tenuous a manner to be considered as "relating to" such plans. The Respondents' claims for fraud arose from the employment relationship between the Petitioner (employer) and Respondents (employees). The Respondents alleged the violation of the Petitioner's duties as an employer, rather than the violation of duties created by an employee benefit plan.

The Petitioner as the Respondents' employer was the only defendant; neither the employee stock ownership plan nor the plan's administrator were parties to this case. The award of damages by the Alabama Courts to the Respondents on their state law fraud claims does not alter the terms of the employee stock ownership plan; the damages the Petitioner as employer would pay to the Respondents as employees for fraud would not come out of the plan's funds. *See Martori Bros. Distributors v. James-Massengale*, 781 F.2d 1349, 1358 (9th Cir. 1986).

The cases relied on by Petitioner in support of his contention that the Respondents' state law fraud claims were preempted by ERISA arose in a dissimilar context

from the present case, and thus are distinguishable from the present case. *Dependahl v. Falstaff Brewing Corp.*, 653 F.2d 1208 (8th Cir. 1981); *Whitaker v. Texaco, Inc.*, 566 F.Supp. 745 (N.D. Ga. 1983); and *Ogden v. Michigan Bell Telephone Co.*, 571 F.Supp. 520 (E.D. Mich. 1983). The plaintiffs in these three cases brought suit in federal court alleging breach of fiduciary duties under ERISA and attached pendent state claims, such as fraud and tortious interference, apparently to avoid ERISA's prohibition against punitive damages. The pendent state claims in these three cases clearly "related to" an employee benefit plan, and the federal courts correctly held that these claims were preempted under ERISA.

State courts, however, that have considered an employee's claim against his employer for breach of the employer's duties *as an employer* have held that the employee's state law claim was not preempted under ERISA. For example, in a case similar to the present case, *Shaver v. N.C. Monroe Constr. Co.*, 63 N.C. App. 605, 306 S.E.2d 519, 523 (1983), the court found that the employee's state law claim against his employer for fraud was not preempted by ERISA. The employer in *Shaver* had fraudulently misrepresented "the continued existence of a pension plan for the purpose of inducing Plaintiff to remain with defendant and to forego bonuses and salary increases." 306 S.E.2d at 523. The court held that the pension plan was "only incidentally or tangentially involved" in the employee's fraud claim against his employer, and ERISA did not preempt the employee's fraud claim. *Id.*

In *Shaw v. Westinghouse Electric Corp.*, 276 Pa.Super. 220, 419 A.2d 175, 179 (1980), the employer alleged that the employee's state law claim for breach of an em-

ployment contract was preempted by ERISA. According to the terms of the employee's contract, the employee would receive a pension based upon 60% of his salary, but the employer refused to pay the employee promised salary increases, thus causing him to lose bonuses and pension benefits. 419 A.2d at 179.

The court recognized that the employee's suit against the employer related solely to the employer's liability for breach of an employment contract; thus, state law was not preempted under ERISA. *Id.* at 180. The court found that, although it would have to examine the employee's present and future rights under the pension plan to determine whether the employer breached the employment contract, this determination would affect only the rights and liabilities of the parties to the action (employer and employee) towards each other; rights and liabilities under the pension plan would remain unaffected. *Id.* The court used the following example to demonstrate this point:

> "Suppose, for example, Shaw had alleged that while promising to provide him with retirement benefits equal to 60% of his base salary, Westinghouse had established a pension plan that provided retirement benefits equal to only 40% of his base salary. If Shaw sued Westinghouse in assumpsit for breach of its promise to provide retirement benefits equal to 60% of his base salary, his suit would neither directly nor indirectly relate to the pension plan established by Westinghouse. So far as the plan would be concerned, Shaw would be entitled to benefits no greater than 40% of his base salary, and so long as the plan paid that amount, Shaw would have no action against it. Shaw's only action would lie against West-

> inghouse, and that action would in no way affect his rights under the plan."

Id. at 179.

The states have a legitimate and important interest in protecting employees from fraudulent misconduct on the part of the employer arising out of the employment relationship, and an employee's claim for fraud against his employer has traditionally been within the domain of the state courts. ERISA was not meant to shield the employer's misconduct from state law where the employee seeks no relief which impinges upon the employee benefit plan. *See Cornell Mfg. Co., Inc. v. Mushlin*, 70 A.D.2d 123, 420 N.Y.S.2d 231, 236 (1979).

Thus, even if the preemption question had been properly presented to the Alabama courts, the Respondents' state law fraud claims would not have been preempted under ERISA. The Alabama Courts correctly held that the Petitioner breached its duty as an employer in fraudulently concealing material information from its employees concerning the proposed merger in order to effectuate the merger. Any alleged impact upon the employee stock ownership plan was much "too tenuous, remote, or peripheral" to justify a finding that the Respondents' fraud claims against their employer "related to" an employee benefit plan. *Shaw v. Delta Air Lines, Inc.*, 103 S.Ct. at 2901 n. 21.

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CONCLUSION

This Court is without jurisdiction to review this state court decision since the preemption question which the Petitioner seeks to have reviewed was neither raised nor passed upon by the state courts below. This state court judgment was decided solely on the basis of state law, and no substantial federal question was presented. Even if the preemption question had been properly presented, however, Respondents' fraud claims against their employer, the Petitioner, would not have been preempted under ERISA because any purported impact on the employee stock ownership plan was "too tenuous, remote, or peripheral."

Accordingly, the Petition for Certiorari should be denied.

Respectfully submitted,

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